



APPRAISAL BULLETIN

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THREE VALUES

SINCE our last two Appraisal Bulletins were devoted to calculating replacement cost by the cubic foot and the square foot methods, it may be in order to consider the application of these methods to the three key values with which the real estate appraiser is most vitally concerned.

THREE KEY VALUES

The prices of these three values are established in three distinct markets, namely: the construction market, the income market and the exchange market. These three markets determine the value or cost of replacement, the rent or price of use and the price in exchange or market price. From the prices established in these three markets the appraiser possesses the basis for determining MAXIMUM VALUE, VALUE and MARKET VALUE. The appraisal of all types of real properties involves all of these three values.

Maximum Value, which includes the sum of the value of the land for its highest and best use, the replacement cost of the improvements and other unique values (such as historic values, etc.), represents the ceiling above which VALUE cannot go, based on the theory that the value of any property cannot be greater than the cost to replace it. (See "A" on appraisal work sheet III, page 306.)

Value is the capitalized sum or the present value of all future benefits of a property. VALUE is sometimes described as the price at which a seller would be justified to sell or a buyer would be justified to buy, regardless of whether actual conditions would warrant a price below or above VALUE. VALUE is also frequently synonymous with long-term investment value, stabilized value, justified value, etc. Either with or without such designations, VALUE is the most important item an appraiser is called upon to appraise. With certain special use properties whose use is not readily measurable by rent, VALUE is determined from MAXIMUM VALUE less the depreciation accrued during the expended useful life of the property. (See "B" on appraisal work sheet III, page 306.)

The third important value, Market Value, represents the price that the property would bring as the result of a voluntary sale if the property were placed on the market. MARKET VALUE frequently carries with it a "surplus discount" (in a distressed market) or a "scarcity premium" (in a scarcity market). This "surplus discount" is the amount deducted from the appraised value due to an oversupply of similar buildings, whereas the "scarcity premium" is the amount added to the appraised value by virtue of a scarcity of similar types of buildings. (See "C" on appraisal work sheet III.)



APPRAISAL WORK SHEET - II
CONSTRUCTION COST

ADDRESS OF PROPERTY St. Louis County, Missouri APPRAISAL NO. Aug. 15, 1948
MADE FOR Mr. John Doe AS AT Aug. 15, 1948

MADE Aug. 15, 1948

MINOR IMPROVEMENTS ON LAND

WALKS	concrete	400	SQFT @	25¢	100-	
DRIVES			SQFT @			
FENCES			L.F. @			
SODDING			SQ YDS @			
WALLS						
GARDENS						
SHRUBS						
ORCHARDS						
MISCELLANEOUS	concrete ash pit				90-	\$ 190-

MAIN IMPROVEMENTS

PROPOSED

DESCRIPTION A two story and full basement frame residence with frame interior with three rooms and lavatory on first floor, and three rooms and bath on second floor. One-car frame garage attached.

TYPE Residence AGES New

SPECIFICATIONS

SIZE	CONSTRUCTION					
	BLDG FRAME	frame	SEPTIC TK	none		
BSMT	full	FOUNDNS	12" reinf. conc.	ROUGH PLBG	modern	
PENT HS	-	BSMT FL	3 1/2" concrete	PLBG FIXT	modern	
STORIES	2	STORES	frame	TYPE HEAT	forced warm air	
OFFICES	-	ROOF	asphalt shingle	HEAT'G PT	Standard	
GARAGES	1	METAL WK.	copper	MECH STKR	-	
DW UNITS	1	INT PARTNS	plaster	OIL BURN	-	
FULL RMS	6	SPEC WALLS	-	GAS FIRED	-	
EFF RMS	-	INT TRIM	yellow pine	WATER HTR	gas fired automatic	
KITCHENS	1	DOORS	2 panel 1 3/8" gum	AIR COND	blower & filters	
KITCHENETTES	-	FLOORS	cl. pl. red oak 7/8"	INSUL'N	4" rockwool wall & ceil.	
DINETTES	-	SPEC FLS	tile in bath & lav	SPRINKLER	-	
SUN RMS	-	TILE	wuct. bath & lav.	SKYLIGHTS	-	
BATHS	1	CEIL'S	plaster	ELEV	-	
LAVATORIES	1	HDWE	A.	FIRE ESC	-	
HEAT'G PLTS.	1	ELECT WK	modern	REFRIG	-	
		ELECT FIXT	A.	GAS STOVES	-	
		SCREENS	copper	BEDS	-	
BLDG HGT	28'	W STRIP	metal	CAB & FANS	built in	
BLDG AREA	907	AWNINGS	-	FRONT POR	8' x 10' conc.	100-
	SQ FT	STOREFRONTS	-	REAR POR	4' x 4' conc.	25-

REPRODUCTION COSTS

MAIN BLDG COST	CUBIC CONTENT	25,376	CUFT @	55	13,900-	
"	"	"	CUFT @	6		\$ 14,025-
SEPARATE GARAGE NO CARS	one	UTILITIES	WATER <input type="checkbox"/>	SEWER <input type="checkbox"/>	LIGHT <input checked="" type="checkbox"/>	HEAT <input type="checkbox"/>
WALLS	frame	ROOF	COMP.	FLOOR	CONC.	SPCL DOORS @
COST OF GARAGE AREA	200	HT	10'	CUBIC CONTENT	2000	CUFT @ 25
OTHER IMPROVEMENTS						\$ 500-
CONSTRUCTION COST NEW						\$ 14,715-
ARCHITECT'S FEES, FINANCING, INTEREST, OTHER COSTS						\$ 835-
REPRODUCTION COST NEW						\$ 15,550-

CODE - G-GOOD; GA-GOOD TO AVERAGE; A-AVERAGE; AP-AVERAGE TO POOR; P-POOR

At this point it will be helpful to distinguish between Market Value and Market Price. The following definitions are adapted from those published by the American Institute of Real Estate Appraisers:

MARKET PRICE - The price paid for a property; the amount of money that must be given or which may be obtained at the market in exchange under the immediate conditions existing at a certain date, regardless of pressures, motives or intelligence. To be distinguished from "Market Value."

MARKET VALUE - The highest price estimated in terms of money which a property will bring if exposed for sale by a willing and well-informed seller in the open market allowing a reasonable time to find a willing purchaser who buys with knowledge of all the uses to which it is adapted and for which it is capable of being used.

The essential difference between "Market Price" and "Market Value," as above defined, lies in the premises of intelligence, knowledge, and willingness, all of which are contemplated in "Market Value" but not in "Market Price." Stated differently, at any given moment of time "Market Value" connotes what a property is actually worth and "Market Price" what it may be sold for. The amounts may or may not coincide, since current supply and demand factors enter strongly into "Market Price."

Of these three values determined from prices in three different and distinct markets, **VALUE** and **MARKET VALUE** are the most important and fundamental in concept. The former is the worth of a property from use and the latter represents its worth to command money in exchange. **MAXIMUM VALUE** is of great importance, being a base or key value from which **VALUE** is often calculated; it is of more importance to the appraiser, however, than to the public.

MAXIMUM VALUE

In the determination of **MAXIMUM VALUE**, the appraiser must determine (a) the value of the land for its highest and best use; and (b) the estimated cost to reproduce the existing improvements under existing market conditions.

HIGHEST AND BEST USE

The highest and best use of the land is its most profitable use or that use which would create the greatest net return applicable to the land. In a great majority of cases, the actual development and use of the land is found to be its highest and best use. This is readily discernible to the experienced appraiser. In some localities that are undergoing a transition from an actual to a higher use,



APPRaisal WORK SHEET-III
APPRaisal-NON INCOME BASIS

ADDRESS OF PROPERTY St. Louis County, Missouri APPRAISAL NO. Aug. 15, 1948
MADE FOR Mr. John Doe MADE Aug. 15, 1948

ECONOMIC CONDITIONS AFFECTING VALUE

TYPE OF CONSTRUCTION frame with frame interior GRADE OF CONSTRUCTION FOR TYPE good
GRADE OF CONDITION FOR AGE new (SEE LIST OF NECESSARY REPAIRS)
STRUCTURAL FAULT crack in foundation wall
REMODELING AND MODERNIZATION none DATE
DISUSED ARCHITECTURAL STYLE AND DESIGN none
EXCESS IN LAYOUT AND CAPACITY none
OBSOLETE EQUIPMENT none
SITE LAYOUT-COVERAGE %
UNDESIRABLE FEATURES OF LIVABILITY closets too small and too few
UNUSALABLE WHIMS IN DESIGN several unusual electronic devices (i.e., automatic door opener)
RELATION OF PRESENT USE TO ZONED USE CONFORMING NON CONFORMING
RELATION OF PRESENT IMPROVEMENTS TO SURROUNDING PROPERTIES OVER IMPROVED CONFORMING UNDER IMPROVED
RELATION OF CLASS OF IMPROVEMENTS TO SURROUNDING STANDARD OF LIVING ABOVE CONFORMING BELOW
IMPROVEMENTS INADEQUATE TO JUSTIFY LAND VALUE DETERMINED FROM HIGHER USE
ASSESSED VALUE: LAND \$ 108 IMPROVEMENTS \$ 170 TOTAL \$ 170 Est. TAXES 18
OCCUPANCY OWNER TENANT VACANT RENTS

APPRaisal

PRESENT VALUE OF LAND - SHEET I 75 feet @ 50- per foot \$ 3,750-
REPRODUCTION COST NEW OF IMPROVEMENTS - SHEET II \$ 15,330-
TOTAL REPRODUCTION VALUE (MAXIMUM VALUE) \$ 19,080-

NECESSARY REPAIRS		ACCrued DEPRECIATION		
ITEM	AMOUNT	ITEM	PERCENT	AMOUNT
NORMAL WEAR AND TEAR				
EXCESSIVE DETERIORATION FOR AGE				
STRUCTURAL FAULT SEE NOTES		STRUCTURAL FAULT SEE NOTES	6.0	930-
PHYSICAL DETERIORATION		PHYSICAL DETERIORATION		930-
OBsolete BUILDING		OBsolete EQUIPMENT		
OBCESS CAPACITY		OBSOLESCENCE		
MISPLACED IMPROVEMENTS		MISPLACED IMPROVEMENTS		
UNDESIRABLE LIVABILITY		UNDESIRABLE LIVABILITY	4.0	620-
UNUSALABLE FEATURES		UNUSALABLE FEATURES	10.0	1,550-
UNDESIRABLE DESIGN		UNDESIRABLE DESIGN		2,170-
INACCESSIBILITY		INACCESSIBILITY		
INCONGRUOUS WITH PROPERTIES AND USES		INCONGRUOUS WITH PROPERTIES AND USES		
INCOMPATIBLE WITH STANDARD OF LIVING		INCOMPATIBLE WITH STANDARD OF LIVING		
NON CONFORMITY TO ENVIRONMENT		NON CONFORMITY TO ENVIRONMENT		
TOTAL NECESSARY REPAIRS	\$			
TOTAL LOSS ACCRUED DEPRECIATION				
LOSS FROM INADEQUATE LAND USE				
LOSS FROM UNFAVORABLE LEASE <input type="checkbox"/> FROM EXCESSIVE TAXES <input type="checkbox"/>				
TOTAL LOSS IN WORTH				
TOTAL GAIN IN WORTH		HISTORICAL <input type="checkbox"/> FAVORABLE LEASE <input type="checkbox"/> FAVORABLE TAXES <input type="checkbox"/>		

APPRaised VALUE (PRESENT WORTH)		scarcity premium
MARKET VARIABLE	ADDITION <input checked="" type="checkbox"/>	DEDUCTION <input type="checkbox"/> NONE <input type="checkbox"/>
MARKET VALUE AFTER REPAIRS		
NECESSARY REPAIRS		
APPRaised MARKET VALUE		

CODE: G-GOOD; GA-GOOD TO AVERAGE; A-AVERAGE; AP-AVERAGE TO POOR; P-POOR

considerable study is necessary before the appraiser can reach a logical conclusion.

There are several questions which the appraiser must answer to his own satisfaction before appraising land for a use higher than its actual use: (1) Is the land restricted in its use by deed or by zoning laws? (2) Does the proposed higher use appear to be the most logical and the most profitable use of the land after a detailed study of the location and its environment? (3) Do population growth or probable shifts in population and the surplus of like use space in the locality warrant the development of the land for this higher use in the immediate future or would they indicate such higher use in the distant future? (4) Do current sales of similar land tend to justify the appraised value of the land for such higher use? Prices obtained in some period in the past or the present asking prices are not a true indication of present value. In general, only conclusions which are based upon reasonable probabilities should be drawn; the consideration of possibilities leads to wishful thinking.

Frequently the appraiser is faced with an apparently "shifting" highest and best use. For instance, at certain times in the real estate cycle the highest and best use of a piece of downtown property may seem to be a parking lot - at another time the highest and best use may seem to be a one-story "taxpayer." Still further along in the cycle an eight-story office building may seem to fulfill the maximum requirements, and at another time the erection of a 40-story building may seem to be the highest and best use. Naturally, the appraiser cannot choose all of these alternates and close attention should be directed to the real estate cycle, which will frequently help the appraiser choose the highest and best use for the property over the long period.

REPLACEMENT COST

The second item of **MAXIMUM VALUE** is the cost to reproduce the existing improvements or the cost to construct proposed improvements. The cost which the appraiser must determine is that estimated cost which would represent the lowest and best bid, had several competent contractors submitted bids to reproduce the existing improvements in the existing market. It is proper to add to construction costs such items as architect fees, taxes and insurance during construction, financing fees, etc., in estimating reproduction cost. Marketing costs are usually not included as a part of reproduction cost, but in theory the inclusion is justified. The greater his experience and the closer his contacts with material and labor costs, the more accurate will be the appraiser's estimate; however, it is well known that competent contractors' bids on identical plans and specifications in the same market show a large spread between the high and the low bid.

METHODS OF ESTIMATING

There are several methods in estimating replacement cost. The most accurate method is that employed by the contractor who takes off bills of materials, estimates hours of labor and secures bids from subcontractors on those parts of construction which require specialized skill, such as plumbing, heating, tile work, plastering, etc. This is a lengthy and expensive method and cannot profitably be used by the appraiser for general practice in his determination of **MAXIMUM VALUE**.

The method next in accuracy is the unit cost method whereby the finished quantity of each type of construction is figured (such as foundation walls and brick walls, floors, partitions, etc.) and a unit cost applied to each. This is also a slow method and requires the appraiser to keep accurate records of unit costs for many types of construction. It is quite expensive if the appraiser uses this method exclusively in his appraisal work; however, it becomes necessary to use this method in part when properties vary from normal types.

One of the better books on the above two methods is the Building Estimator's Reference Book published by Frank R. Walker Company, Chicago, Illinois.

A short-cut method is the application of a cubic foot cost to the actual cubic content of the building. The degree of accuracy in this method depends upon the care used in measuring the property and in estimating cubic content and upon the accuracy and appropriateness of up-to-date cubic foot costs possessed by the appraiser. We have discussed the method of arriving at cubic content and square foot area in the two preceding bulletins.

One very valuable aid to our appraisal department are the up-to-date costs on several types of buildings kept by our research department. The research department estimates costs on various types of buildings each month by pricing (dealer-to-contractor, delivered-to-job price) all items in each building's bill of materials, and by obtaining current wage information and subcontractor overhead and profit figures from companies actively engaged in the building industry. The costs thus obtained are divided by the cubic content of the building in order to find the cubic cost. These cubic costs are used by our appraisal department as a yardstick to measure cubic costs on similar type buildings. On page 309 is a table showing the changes in costs of our standard six-room frame house from 1913 through July 1948. This is excellent material to use on an index basis to find the increase in construction costs for a two-story frame house. The cubic cost of the house is shown for several periods in the right-hand margin of the page. Most of the data necessary to estimate reproduction costs are found on our appraisal work sheet II on page 304. The total reproduction cost of a building very similar to the standard six-room frame house is \$15,550 (August 15, 1948). This cost includes garage, front and rear concrete stoops, concrete walks, architect fees, financing fees, etc. Appraisal work sheet III shows the value of the land to be \$3,750; therefore, the maximum value of the property was \$19,300. Certain depreciating influences (detailed on appraisal work sheet III) cause deductions of \$3,100 from maximum value. Thus the value (or appraised value) is \$16,200. To this value is added a scarcity premium of \$800, giving a market value of \$17,000.

If it were not for the depreciating influences in connection with the property, the maximum value figure would be the same as the value figure but not necessarily the same as the market value. (Market value might vary by the amount of scarcity premium or the surplus discount.) This method, while applied to a small residence for illustrative purposes, is the same for all types of properties, regardless of size.

